

DEPARTMENT OF WATER RESOURCES

California Energy Resources Scheduling
PO Box 219001
3310 El Camino Avenue, Suite 120
SACRAMENTO, CA 95821-9001
(916)574-1291



February 28, 2002

Southern California Edison Company
8631 Rush Street
Rosemead, CA 91770
Attention: James Scilacci

Dear Mr. Scilacci:

This Letter Agreement (this "Letter Agreement"), effective on date of execution, is being entered into by and between the California Energy Resources Scheduling division of the California Department of Water Resources ("CDWR"), acting solely under the authority and powers granted by AB1-X, codified as Sections 80000 through 80270 of the California Water Code, as amended (the "Act"), including but not limited to its authority to make payments from amounts in the Department of Water Resources Electric Power Fund (the "Electric Power Fund") available for the purposes set forth in this Letter Agreement, but not under its powers and responsibilities with respect to the State Water Resources Development System, and Southern California Edison Company, a corporation organized and existing under the laws of the State of California ("SCE"). The Act, together with any subsequent legislation which extends such authorization, is referred to herein collectively as the "Extended Act."

This Letter Agreement is being entered into by CDWR and SCE to address CDWR's and SCE's respective rights and obligations with respect to (a) real-time electric energy used to serve SCE's retail load that has not been, and is not, served by SCE generation resources and contracts in any hour since Hour Ending 2200 (10:00 p.m.) (the "last SCE cost responsibility hour") on January 17, 2001 ("Imbalance Energy"); provided that whether Instructed Imbalance Energy (as defined in the ISO tariff) provided by SCE generation and contracts to the ISO in real-time shall be considered to serve SCE's retail load, and hence considered to be Imbalance Energy hereunder, shall be treated in accordance with Section 3 herein, and (b) certain other costs relating specifically to SCE invoiced to CDWR ("Other ISO Invoiced Charges" and collectively with Imbalance Energy costs, the "ISO Invoiced Charges") by the California Independent System Operator Corporation (the "ISO") pursuant to that certain Federal Energy Regulatory Commission ("FERC") order dated November 7, 2001 (Docket Nos. ER01-3013 and ER01-889). CDWR and SCE (each a "Party" and collectively the "Parties") are entering into this Letter Agreement with the principal understanding that (a) each Party will have the ability to recover revenues from SCE's retail customers through appropriate regulatory or judicial proceedings sufficient to cover that Party's financial responsibility for such appropriate portion of the ISO Invoiced Charges and (b) the allocation of financial responsibilities as set forth in Exhibits A-1 and A-2 of this Letter Agreement will not cause double-billing of SCE's retail customers for the ISO Invoiced Charges.

As authorized under the Act and other authorizing acts, commencing on the last SCE cost responsibility hour on January 17, 2001, CDWR has procured electric energy to serve SCE's retail load that has not been, and is not, served by SCE generation resources and contracts. The Parties wish to clarify the allocation of financial responsibility for the cost of a portion of such procured electric energy constituting Imbalance Energy and further clarify the allocation of financial responsibility for the Other ISO Invoiced Charges. This Letter Agreement allocates financial responsibilities for disputed items noted in CDWR's December 7, 2001 FERC Request for Rehearing ("Request for Rehearing") and costs due and payable with respect to the ISO Invoiced Charges, and the Parties are entering into this Letter Agreement to fully and finally settle the outstanding disputes noted in CDWR's Request for Rehearing as such disputes relate to SCE; provided, however, nothing in this Letter Agreement is intended to release or extinguish any rights of CDWR or SCE to file disputes with the ISO related to the ISO invoices or the related settlement data which do not relate to the allocation of charges between the Parties as set forth in Exhibits A-1 and A-2 attached hereto. Upon CDWR's receipt of all Catch-Up Remittances (defined below) provided in Section 1 herein and the Other ISO Charge Remittances (defined below) provided in Section 2 herein, CDWR shall acknowledge that all disputes it has filed to date with the ISO relating to the allocation of financial responsibilities as provided in Exhibits A-1 and A-2 of this Letter Agreement would be fully and finally settled. In addition, this Letter Agreement clarifies the remittance obligations of SCE from its ratepayers on behalf of CDWR for Imbalance Energy used to serve SCE's retail load and CDWR's and SCE's agreed responsibility for the designated ISO Invoiced Charges.

In consideration of the mutual promises and undertakings of the Parties set forth herein, the Parties hereby agree as follows:

SECTION 1. CDWR Payment of Imbalance Energy Costs and SCE Remittance of Related Revenues to CDWR. Pursuant to the November 7, 2001 FERC order, CDWR has received invoices from the ISO for ISO Invoiced Charges, including costs related to Imbalance Energy. Upon effectiveness of this Letter Agreement and during the term of this Letter Agreement as provided in Section 14 hereof, after the last SCE cost responsibility hour, CDWR shall be responsible for the procurement cost for Imbalance Energy delivered to SCE's retail customers and associated costs and for those charges allocated to CDWR in Exhibit A-1 hereto and pursuant to the terms of item 8 in Exhibit A-2 hereto.

During the term of this Letter Agreement, after the last SCE cost responsibility hour, SCE shall have no financial responsibility related to the procurement of such Imbalance Energy or other charges for which financial responsibility has been accepted by CDWR as set forth in Exhibit A-1 and pursuant to the terms of item 8 in Exhibit A-2.

SCE, however, shall be obligated to make remittances ("Imbalance Energy Remittances") to CDWR at the appropriate rate determined by the CPUC pursuant to the methodology for payment described in this Letter Agreement, the Servicing Agreement executed between the Parties as of June 23, 2001, as may be amended (the "Servicing Agreement"), and relevant CPUC orders.

SCE and CDWR acknowledge CPUC Decision 02-02-052 and agree to acknowledge any subsequent CPUC decisions affecting the rate paid to CDWR for power deliveries to SCE's retail customers. The Parties agree to make any payment adjustments necessary to reflect any difference between the Imbalance Energy Remittances due to CDWR at the applicable CPUC interim rates as described in Exhibits B and C and the Imbalance Energy Remittances that are due based on the CPUC's retroactive rate for the same period determined in CPUC Decision 02-02-052 or any other relevant CPUC order in accordance with the provisions and timing specified in such order.

For purposes of calculating Imbalance Energy Remittances for the period after the last SCE cost responsibility hour on January 17, 2001, the quantities of Imbalance Energy shall be determined based on the methodology as described in Exhibit B hereto and Section 3 herein.

Unless otherwise ordered by the CPUC, SCE shall make remittances for Imbalance Energy for the period beginning January 17, 2001 through the date of the execution of this Letter Agreement (the "Catch-up Period," and such remittances are herein referred to as "Catch-up Remittances") in monthly installments to be paid beginning on April 1, 2002, and continuing on the first business day of each succeeding month as follows:

April 1, 2002	\$100 million
May 1, 2002	No payment
June 3, 2002	\$150 million
July 1, 2002	Remaining amount owing for Catch-Up Remittances

The amount owed for Imbalance Energy for the Catch-up Period shall be equal to the Imbalance Energy Catch-up Payable as determined in accordance with Exhibit B attached hereto. The total amount of Catch-up Remittances to be paid by SCE in four monthly installments shall equal the Imbalance Energy Catch-up Payable minus the Total Offsets as determined in accordance with Exhibit C attached hereto ("Catch-Up Remittances Before Interest"), plus the interest described in this paragraph. Interest on Catch-Up Remittances Before Interest shall be calculated at the Goldman Sachs Financial Square Money Market Fund daily rate (the "SCE Daily Money Market Rate"), compounded daily, on amounts owed beginning forty-five (45) days after the day the energy was delivered and ending on the date paid. The SCE Daily Money Market Rate shall be provided by SCE for each day in the Catch-up Period, and for each day after the date of the execution of this Letter Agreement on a monthly basis for as long as outstanding payables are owed hereunder. Each payment by SCE of the Catch-Up Remittances as set forth in this Section shall reduce the principal amount upon which interest is calculated for subsequent payment periods. SCE may pay any remaining balance ahead of the schedule indicated above without penalty.

The Parties agree to revise Attachment H to the Servicing Agreement as part of the Amendment to the Servicing Agreement (as described in Section 9 herein) within fifteen (15) business days of the date of execution of this Letter Agreement in order to incorporate into the calculation of the daily DWR Percentage, as defined in Attachment

H of the Servicing Agreement, both forecast Imbalance Energy and the difference between forecast and actual Imbalance Energy. The Parties agree to make such revision to Attachment H effective on the day that such Amendment to the Servicing Agreement is approved by the CPUC. From the day after the effective date of this Letter Agreement through the day before such Amendment to the Servicing Agreement is effective (the "Transition Period"), SCE shall calculate remittances due to or from CDWR for Imbalance Energy using the methodology contained for calculations for the Imbalance Energy Catch-up Payable described in Exhibit B hereto. The Parties agree to settle on and make payments for the net amount owed for Imbalance Energy for the Transition Period ninety days after the end of the Transition Period, including interest at the SCE Daily Money Market Rate, compounded daily, beginning 45 days after the day Imbalance Energy was delivered and ending on the date of payment. In that connection, SCE agrees to comply with all provisions related to collection and segregation requirements as set forth in the Act and in accordance with the remittance methodology contained in the Servicing Agreement.

SECTION 2. Other ISO Invoiced Charges. CDWR agrees to accept financial responsibility for those portions of Other ISO Invoiced Charges, after the last SCE cost responsibility hour, for which CDWR is identified as the responsible party in Exhibit A-1 and pursuant to the terms of item 8 in Exhibit A-2. In addition, SCE agrees to accept financial responsibility for those portions of Other ISO Invoiced Charges for which SCE is identified as the responsible party in Exhibit A-2.

In the event that the ISO or another entity responsible for the maintenance of grid reliability and transmission service were to change the calculation of any charge type or adds new charge types, the Parties agree to enter into good faith negotiations to determine responsibility for such changed or new charge type in a manner consistent with the principles that a) each Party will have the ability to recover revenues from SCE's retail customers through appropriate regulatory or judicial proceedings sufficient to cover that Party's financial responsibility for such appropriate portion of the ISO Invoiced Charges and (b) the allocation of financial responsibilities as set forth in Exhibits A-1 and A-2 of this Letter Agreement will not cause double-billing of SCE's retail customers for the ISO Invoiced Charges.

SCE shall reimburse CDWR for amounts previously paid to the ISO in respect of Other ISO Invoiced Charges allocated to SCE in Exhibit A-2, including Charges for Non-Retail Load as determined pursuant to Section 4 hereunder, for the period January 17, 2001 through the December 2001 preliminary ISO invoice ("Other ISO Charge Remittances"), and including any associated interest CDWR has paid to the ISO with respect to those amounts so that the accrued interest paid by the Parties for such charge types correlates to the assumed financial responsibility of each Party as provided herein. With respect to Other ISO Charge Remittances, SCE and CDWR agree to confer as to the amount of Other ISO Charge Remittances allocated to SCE within forty-five (45) days after the execution of this Letter Agreement. Upon CDWR's and SCE's joint determination of such amounts, SCE shall remit Other ISO Charge Remittances for Other ISO Charges previously paid by CDWR as a lump sum no later than September 1, 2002. SCE shall also pay to CDWR accrued interest on such Other ISO Charge Remittances from the date paid by CDWR to the ISO to the date

reimbursed by SCE to CDWR, at the SCE Daily Money Market Rate, compounded daily.

With respect to Other ISO Invoiced Charges allocated to SCE in Exhibit A-2, including Charges for Non-Retail Load determined pursuant to Section 4 herein, which have not been previously paid by CDWR to the ISO, SCE shall, from and after the effective date hereof, pay CDWR an amount equal to SCE's portion of Other ISO Invoiced Charges and CDWR shall remit the same amount to the ISO as payment for such Other ISO Invoiced Charges. With respect to ISO invoices received after the effective date of this Letter Agreement, SCE and CDWR agree to confer as to the amount of ISO monthly invoice charges allocated to each Party within 3 business days after receipt of the invoice from the ISO. Upon CDWR's and SCE's joint determination of such amounts consistent with the allocation set forth in Exhibits A-1 and A-2 attached hereto, SCE shall remit its respective portion of the Other ISO Invoiced Charges to CDWR on the same schedule as CDWR payments are due to the ISO in accordance with the ISO Payments Calendar (as defined in the ISO tariff). In the event that SCE does not make such remittances in full when due, SCE shall pay interest on the amount owed at the interest rates specified in the following sentence, compounded daily, from the due date to the date that payment is made. The applicable interest rate for this determination shall be the SCE Daily Money Market Rate for the first 30 days after amounts are due to the ISO, and the Late Payment Rate, as defined in the Servicing Agreement, for the period of time beginning 30 days after the amounts are due to the ISO until paid. Moreover, in the event that the ISO provides separate invoices to CDWR and SCE for ISO charges that are inconsistent with the financial responsibility allocation contained in Exhibits A-1 and A-2, the Parties agree to coordinate in the payment of such invoices and make any payment adjustments between themselves that are necessary to implement the financial responsibility allocation contained in Exhibits A-1 and A-2, to the extent allowed by applicable law.

Upon effectiveness of this Letter Agreement and during the term of this Letter Agreement as provided in Section 14, each Party shall be responsible for its respective portion of the Other ISO Invoiced Charges as set forth in Exhibits A-1 and A-2 hereto.

SECTION 3. Instructed Imbalance Energy. The Parties have not reached agreement regarding the treatment of Instructed Imbalance Energy as defined in the ISO tariff ("Instructed Imbalance Energy") and regarding whether Instructed Imbalance Energy provided by SCE generation and contracts to the ISO in real-time should be considered to serve SCE's retail load, and hence considered to be Imbalance Energy hereunder. Upon the execution of this Letter Agreement, SCE shall promptly seek clarification from the CPUC regarding the treatment of Instructed Imbalance Energy and whether Instructed Imbalance Energy provided by SCE generation and contracts to the ISO in real-time shall be considered to serve SCE's retail load, and hence should be considered Imbalance Energy for purposes of calculating remittances hereunder. Upon such clarification by the CPUC, the Parties shall apply the methodology adopted by the CPUC to the remittance obligations hereunder, and the Parties shall reimburse each other as necessary to adjust the amounts paid or owing by either Party based on the methodology approved by the CPUC, including interest on such adjustment at the SCE Daily Money Market Rate, compounded daily. However, until the CPUC issues a

decision on the treatment of Instructed Imbalance Energy, and for the purposes of making any payments when due hereunder, the Parties agree to the following:

(A) For purposes of calculating Imbalance Energy Remittances, Instructed Imbalance Energy produced from SCE's URG and contracts shall be considered sold by SCE to SCE's retail customers, and Instructed Imbalance Energy that is a reduction in the quantity of SCE's URG and contracts shall be considered to (a) reduce the amount of energy available from SCE's URG and contracts to serve SCE's retail load and (b) may result in additional energy being required to serve SCE's retail load that is considered to be purchased by CDWR from the ISO and sold by CDWR to SCE's retail customers; and

(B) Remittances by SCE for ISO Invoiced Charges shall not include charges or credits for Instructed Imbalance Energy provided by SCE.

The Parties agree that the above-described interim treatment of Instructed Imbalance Energy shall be without prejudice to either Party's position with respect to this issue.

SECTION 4. Charges for Non-Retail Load. In order to determine cost responsibility with respect to Charges for Non-Retail Load (as described in item 8 of Exhibit A-2), on a monthly basis SCE agrees to provide CDWR with SCE's cost allocation for each Existing Transmission Contract and SCE Power Contract (listed on Exhibit D). SCE's cost allocation shall identify all of the ISO credits and costs applicable to each Existing Transmission Contract or SCE Power Contract including, but not limited to, those ISO Invoiced Charges identified in Exhibit A-1 and A-2 for each hour. In addition, SCE agrees to provide all ISO Charge Type 401 and 407 energy quantities relating to each Existing Transmission Contract or SCE Power Contract. SCE agrees to provide this information for the months of January through November 2001 30 days following execution of this Letter Agreement. For each succeeding month, SCE agrees to provide such information 30 days after the due date for the payment of ISO charges for that month. Collectively, the information provided by SCE under this paragraph, as well as applicable ISO settlements data relating to this information, shall be defined as "Non-Retail Load Settlement Information".

SCE shall provide to CDWR, within ten (10) business days after the execution of this Letter Agreement, a list of the Existing Transmission Contracts and Power Contracts listed on Exhibit D hereto, containing the dates of execution and full names of the Parties thereto. SCE further agrees to provide CDWR, within ten (10) business days after the execution of this Letter Agreement, a description of the processes used to allocate ISO charges and credits to Existing Transmission Contracts and Power Contracts. SCE agrees to (1) allocate ISO charges and credits to Existing Transmission Contracts and Power Contracts in a manner that is consistent with the ISO's method for allocating such charges and credits and (2) use the same allocation process for the purposes of this Letter Agreement as SCE uses for other contracts and for internal accounting and regulatory reporting purposes.

SECTION 5. Settlement Information. Pursuant to the November 7, 2001 FERC order, the Parties agree that CDWR has received or will receive (a) Final Settlement Statements for the period beginning January 17 through September 30, 2001 from the

ISO relating to ISO Scheduling Coordinator identification SCE1, (b) Preliminary and Final Settlement Statements for dates on and after October 1, 2001 from the ISO relating to ISO Scheduling Coordinator identification SCE1, and (c) Non-Retail Load Settlement Information pursuant to Section 4 above (collectively, the "Settlement Information"). The Parties agree to treat the Settlement Information as Confidential Information, as defined in the Servicing Agreement, in accordance with Section 6.1 of the Servicing Agreement.

The Parties contemplate that the State Controller, Bureau of State Audits, or other entities authorized under State law to verify expenditure of public funds relating to the activities authorized under the Extended Act may need to have access to confidential Settlement Information received by CDWR. Upon receipt of such request, CDWR will provide a written notice of such request to SCE, and SCE agrees that in the exercise of its reasonable discretion it will provide CDWR with written consent to make available all or a portion of the confidential Settlement Information related to SCE to such State entities as soon as reasonably practicable, provided that any such State entity agrees to be bound by the terms and conditions and the intent set forth in this Section 4 or another agreement mutually acceptable to SCE and such State entity regarding the treatment of confidential Settlement Information related to SCE.

To the extent permitted by law, CDWR expressly agrees to maintain confidential treatment of all Settlement Information related to SCE provided under this Letter Agreement when requested to produce any such information pursuant to the California Public Records Act. Upon receipt of any request for such Settlement Information related to SCE under the California Public Records Act, CDWR will notify SCE in a timely manner and as far as reasonably practicable in advance of disclosure if CDWR determines that it must release such Settlement Information related to SCE provided to CDWR under this Agreement. The Parties will then endeavor to reach agreement as to the intended disclosure, including appropriate redaction of Settlement Information related to SCE so that the document may be disclosed. If the Parties cannot reach a mutually acceptable agreement to allow the disclosure of requested Settlement Information related to SCE, then CDWR will provide SCE with sufficient time to take appropriate action to protect its interests prior to disclosing any such Settlement Information related to SCE.

SECTION 6. Financial Responsibility. Pursuant to this Letter Agreement, CDWR and SCE will jointly notify the ISO as to the financial responsibility and payment arrangements for ISO Invoiced Charges provided hereunder.

It is CDWR's intent to have a consistent settlement agreement to address cost allocation of ISO Invoiced Charges for non-creditworthy investor-owned utilities (IOUs). Should CDWR reach an agreement with respect to the allocation of ISO Invoiced Charges with another non-creditworthy IOU for which it is authorized to procure power under the Act that, in SCE's judgment, is more favorable than the allocation of charges set forth in Exhibits A-1 and A-2 hereto, SCE shall have the right to receive the same allocation of ISO Invoiced Charges as such other IOU to be applied to SCE's agreement with CDWR under this Letter Agreement. This provision explicitly does not permit SCE to select particular portions of such other IOU's allocation of ISO Invoiced

Charges to be applied to SCE's allocation under this Letter Agreement, and if SCE elects to take the allocation of ISO Invoiced Charges of such other IOU's agreement with CDWR, SCE takes such other IOU's allocation in its entirety and shall forgo any rights or benefits under Exhibits A-1 and A-2 hereto.

SECTION 7. Coordination of Settlement and Payment Activities. The Parties agree to coordinate their settlement and payment activities hereunder and exchange relevant information to prevent the double payment of any ISO charge. Although the Parties have no responsibility for the ISO's remittance of revenue to third parties, each Party agrees to advise the other if it becomes aware of any ISO overpayment or duplicate payment to third parties. The Parties agree to work together to promptly reverse any such overpayment or duplicate payment by the ISO.

SECTION 8. Filing of Letter Agreement. CDWR agrees to file an executed copy of this Letter Agreement with FERC for informational purposes within an existing docket as a full and final resolution of the issues raised in CDWR's Request for Rehearing with respect to CDWR's responsibility for ISO Invoiced Charges with respect to SCE as provided in Exhibit A-1 and SCE responsibility for ISO Invoiced Charges as provided in Exhibit A-2. In addition, CDWR at its discretion may file this Letter Agreement with the CPUC so as to update its revenue requirement.

SECTION 9. Amendment to the Servicing Agreement. The Parties agree to enter in an amendment to the Servicing Agreement which will include among its provisions, the same provisions as this Letter Agreement (the "Amendment to the Servicing Agreement") within fifteen (15) business days of the date of execution of this Letter Agreement. The Parties agree that within seven (7) days of the execution of the Amendment of the Servicing Agreement by both Parties, SCE shall file with the Commission a Motion for Expedited Approval of Amendment to the Servicing Agreement. The Parties acknowledge that the CPUC may order amendment to this Letter Agreement as part of its approval of and any change to the proposed Amendment to the Servicing Agreement, and the Parties agree to amend this Letter Agreement as may be ordered by the CPUC.

SECTION 10. Audit Rights. Each Party shall have the right to undertake, or request the undertaking by a competent independent party of an audit of the ISO invoices relating to this Letter Agreement, final settlement data concerning such ISO invoices and Non-Retail Load Settlement Information with regard to any allocation, cost or financial obligation of either Party resulting from this Letter Agreement, the cost of which audit shall be paid by the Party requesting such audit. In addition, CDWR's audit rights as described in Section 8.2 of the Servicing Agreement shall apply to any information required for implementing this Letter Agreement, including the right to audit SCE records and procedures containing information bearing upon SCE's performance of its obligations under this Letter Agreement. The audit rights provided in this paragraph shall extend one year beyond the date of termination of this Letter Agreement.

SECTION 11. No Waiver. The failure to object to a breach of a provision in this Letter Agreement by either Party shall not be deemed to be a waiver of any other rights of such Party contained in this Letter Agreement.

SECTION 12. Good Faith Negotiations Upon Amendment. Upon the effective date of this Letter Agreement, if there is any amendment or modification of a related condition required by any governmental body having jurisdiction, the Parties will enter into good faith negotiations as soon as practicable to develop and enter into a new arrangement which preserves the respective rights, obligations and benefits under this Letter Agreement as nearly as possible.

SECTION 13. Dispute Resolution. Should any dispute arise between the Parties as to the specific amounts to be remitted under Sections 1, 2 and 3 hereof, or should any dispute between the Parties arise from the exercise of either Party's audit rights contained in Section 10 hereof, the Parties shall remit any undisputed amounts and agree to enter into good faith negotiations as soon as practicable to resolve such disputes within (10) business days so as to fully allocate and pay appropriate amounts to each other or to the ISO as appropriate within the timeframes provided under this Letter Agreement, or as soon as possible thereafter. For disputed ISO Invoiced Charges, if such resolution cannot be made before the ISO invoice due date, SCE shall accept and remit the undisputed portion of such ISO Invoiced Charges to CDWR. In addition, CDWR shall pay the disputed portion of the ISO Invoiced Charges to the ISO and SCE shall deposit an amount equal to the disputed portion of the ISO Invoiced Charges into an escrow account held by a qualified, independent escrow holder. SCE shall reimburse CDWR from the escrow account as necessary to reflect the resolution of such disputes.

SECTION 14. ISO Disputes. Nothing in this Letter Agreement is intended to release or extinguish any rights of CDWR or SCE to file disputes with the ISO related to the ISO invoices or the related settlement data which do not relate to the allocation of charges between the Parties as set forth in Exhibits A-1 and A-2 attached hereto. Furthermore, SCE agrees to review all ISO settlement statements pertaining to the SCE1 Scheduling Coordinator and file disputes as necessary.

SECTION 15. Term. Upon the earlier of (a) SCE becoming creditworthy (as defined by the ISO tariff) and obtaining CPUC approval of SCE's resumption of the procurement function for its retail customers or (b) expiration of CDWR's authority under the Extended Act to enter into contracts for the cost of electric power and transmission, scheduling, and other related expenses incurred by CDWR from amounts in the Electric Power Fund available for purposes set forth herein, this Letter Agreement and the rights and obligations of each Party hereunder shall automatically terminate. Upon such event, nothing in this Letter Agreement shall establish, bind or allocate financial responsibility to either Party for ISO Invoiced Charges from such time forward. In addition, this Letter Agreement may be terminated by mutual agreement of the Parties in writing.

SECTION 16. Governing Law. This Letter Agreement shall be construed in accordance with the laws of the State of California. Nothing herein shall be deemed an

admission of, or consent to, the jurisdiction of any court or administrative body by either party with respect to any issue arising under or related to this Letter Agreement, nor as a waiver of any objection either Party may have to the exercise of jurisdiction by, submission to or consideration by any court or administrative body of any such issues, including but not limited to on the basis of the Eleventh Amendment of the United States Constitution, Johnson Act (28 U.S.C. Section 1343) or the United States Bankruptcy Code.

SECTION 17. Assignment. Neither Party shall assign this Letter Agreement or its rights hereunder without the prior written consent of the other Party, which consent may be withheld in the exercise of its sole discretion.

SECTION 18. Severability. In the event that any of the terms, covenants or conditions of this Letter Agreement, or the application of any such term, covenant or condition, shall be held invalid as to any person or circumstance by any court, regulatory agency, or other regulatory body having jurisdiction, all other terms, covenants, or conditions of this Letter Agreement and their application shall not be affected thereby, but shall remain in full force and effect, unless a court, regulatory agency, or other regulatory body holds that the provisions are not separable from all other provisions of this Letter Agreement.

SECTION 19. Limited Liability. Any liability of CDWR arising in connection with this Letter Agreement or any claim based thereon or with respect thereto arising as the result of any breach or default hereunder, and any other payment obligation or liability of or judgment against CDWR hereunder, shall be satisfied solely from the Electric Power Fund. Neither the full faith and credit nor the taxing power of the State of California are or may be pledged for any payment hereunder. Revenues and assets of the State Water Resources Development System shall not be liable for or available to make any payments or satisfy any obligation arising hereunder.

SECTION 20. Counterparts. This Letter Agreement may be executed in one or more counterparts, each of which shall be deemed to be an original, but all of which together shall be deemed to be one and the same instrument.

SECTION 21. Entire Agreement. This Letter Agreement (including the exhibits hereto) constitutes the entire agreement and supersedes all prior agreements and understandings, both written and oral, among the parties with respect to the subject matter hereof.

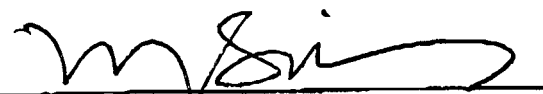
Very truly yours,

CALIFORNIA DEPARTMENT OF WATER RESOURCES, acting solely under the authority and powers granted by AB1-X, codified as Sections 80000 through 80270 of the California Water Code, as amended, and not under its powers and responsibilities with respect to the State Water Resources Development System

By: 
Peter S. Garriss
Deputy Director

ACCEPTED AND AGREED TO
AS ABOVE WRITTEN:

SOUTHERN CALIFORNIA EDISON COMPANY

By: 
James Scilacci
Title: Vice President and Chief Financial Officer
Date: February 28, 2002

SECTION 21. Entire Agreement. This Letter Agreement (including the exhibits hereto) constitutes the entire agreement and supersedes all prior agreements and understandings, both written and oral, among the parties with respect to the subject matter hereof.

Very truly yours,

CALIFORNIA DEPARTMENT OF WATER
RESOURCES, acting solely under the
authority and powers granted by AB1-X,
codified as Sections 80000 through 80270 of
the California Water Code, as amended, and
not under its powers and responsibilities with
respect to the State Water Resources
Development System

By: _____
Peter S. Garriss
Deputy Director

ACCEPTED AND AGREED TO
AS ABOVE WRITTEN:

SOUTHERN CALIFORNIA EDISON COMPANY

By: _____
James Scilacci
Title: Vice President and Chief Financial Officer
Date: February 28, 2002

EXHIBIT A-1

Charge	Responsible Party
<p>1. Ancillary Services: From January 17, 2001 forward, CERS will assume financial responsibility for Ancillary Services (currently CT (Charge Type) 111-Spinning Reserve due ISO; 112-Non-Spinning Reserve due ISO; 114-Replacement Reserve due ISO; 115-Regulation Up due ISO; 116-Regulation Down due ISO).</p> <p>A. Net of IOU Ancillary Service revenue derived from utility retained generation (<i>i.e.</i>, currently CT 1-Day Ahead Spinning Reserve due SC; 2-Day Ahead Non-Spinning Reserve due SC; 4-Day Ahead Replacement Reserve due SC; 5-Hour Ahead Regulation Up due SC; 6-Day Ahead Regulation Down due SC; 51-Hour Ahead Spinning Reserve due SC; 52-Hour Ahead Non-Spinning Reserve due SC; 54-Hour Ahead Replacement Reserve due SC; 55-Hour Ahead Regulation Up due SC; 56-Hour Ahead Regulation Down due SC); 24-Dispatched Replacement Reserve (Bid-In) Capacity Withhold; 124-Dispatched Replacement Reserve (Self-Provided) Capacity Withhold.</p> <p>B. As adjusted by Rational Buyer, RMR Preemption, <i>i.e.</i>, CT 1011-Ancillary Service Rational Buyer Adjustment; 1061-Distribution of Preempted Spinning Reserve; 1062-Distribution of Preempted Non-Spinning Reserve; 1064-Distribution of Preempted Replacement Reserve; 1065-Distribution of Preempted Regulation Up; 1066-Distribution of Preempted Regulation Down; 1012-RMR Preemption Revenue Allocation; 61- Hour Ahead RMR Preemption of Spinning Reserve; 62- Hour Ahead RMR Preemption of Non-Spinning Reserve; 64- Hour Ahead RMR Preemption of Replacement Reserve; 65- Hour Ahead RMR Preemption of Regulation Up; 66- Hour Ahead RMR Preemption of Regulation Down; 71- Real Time RMR Preemption of Spinning Reserve; 72- Real Time RMR Preemption of Non-Spinning Reserve; 74- Real Time RMR Preemption of Replacement Reserve; 75- Real Time RMR Preemption of Regulation Up; 76- Real Time RMR Preemption of Regulation Down; 81- Real Time RMR Preemption of Spinning Reserve; 82- Real Time RMR Preemption of Non-Spinning Reserve; 84- Real Time RMR Preemption of Replacement Reserve; 85- Real Time RMR Preemption of Regulation Up; 86-Real Time RMR Preemption of Regulation Down.</p> <p>C. As further adjusted by No Pay and Noncompliance, <i>i.e.</i>, CT 141-No Pay Charge Spinning Reserve; 142-No Pay Charge-Non-Spinning Reserve; 144-No Pay Charge-Replacement Reserve; 145-Non Compliance Charge for Regulation Up; 146-Non Compliance Charge for Regulation Down; 1030-No Pay Provision Market Refund.</p>	<p>CERS</p>

Charge	Responsible Party
2. Imbalance Energy and UFE: From January 17, 2001 forward, with respect to net short of the IOUs, CERS will assume financial responsibility for Imbalance Energy, <i>i.e.</i> , currently CT 406-SC Unaccounted for Energy; 407-Uninstructed Energy; 487-Allocation of Excess Cost for Uninstructed Energy; 591-Emissions Cost Recovery; and 592-Start-Up Cost Recovery—as netted against current CT 401-Instructed Energy; 481-Excess Cost for Instructed Energy; 593-Emissions Cost Due Trustee; and 594-Start-Up Cost due Trustee revenues received by the IOUs from their utility retained generation.	<i>CERS; however, responsibility for CT 401, 481 Instructed Energy credits and charges to be determined by the CPUC as described in Section 3.</i>
3. Neutrality: From January 17, 2001 forward CERS will assume responsibility for CT 1010-Neutrality; 1210-Existing Contracts Cash Neutrality Charge/Refund.	<i>CERS</i>
4. Interest: CERS will assume responsibility for CT 3999 Interest and Penalty Charges for those charges set forth in Exhibit A-1 and with respect to such charges related to the net short of SCE that CERS has assumed responsibility as set forth in Exhibit A-2. CERS will not pay interest accrued on past due principal amounts prior to January 17, 2001.	<i>CERS</i>

EXHIBIT A-2

Charge	Responsible Party
1. Grid Management Charge: These ISO administrative fees are composed of CT 521-Control Area Services Grid Management Charge; 522-Interzonal Scheduling Grid Management Charge; 523-Market Operations Grid Management Charge; 524-A/S and Real Time Energy Operations Charge; 3351-Grid Management Charge Adjustment Charge/Refund.	SCE
2. Demand Relief Programs: This includes Charge Types 117-Demand Relief Monthly Capacity Charge less 007-Demand Relief Monthly Payment; 3482-Demand Relief Monthly Energy Charge less 3472-Demand Relief Energy Payment; 3483-Discretionary Load Curtailment Program Energy Charge less 3473- Discretionary Load Curtailment Program Energy Payment; 1120-Est. Summer Reliability Contract Capacity Payment/Charge; 1121-Adj. Summer Reliability Contract Capacity Payment/Charge.	SCE
3. Transmission Charges: These Charge Types include 372-High Voltage Access Charge due ISO; 382-High Voltage Wheeling Charge due ISO; 383-Low Voltage Wheeling Charge.	SCE
4. Inter-Zonal Congestion: These Charge Types include 203-Day-Ahead Inter-Zonal Congestion Settlement; 253-Hour-Ahead Inter-Zonal Congestion; 256-Hour-Ahead Inter-Zonal Congestion Debit to SCs.	SCE
5. URG Penalty: This penalty charge (CT 485-Insufficient Response to Alert, Warning and Emergency instruction) is associated with lack of response by utility retained generators in emergency conditions.	SCE
6. Underscheduling Penalty: This penalty charge (CT 480-Under Scheduled Load Penalty-due ISO) is associated with the IOUs' forecast of load.	<i>The Underscheduling Penalty has been eliminated by FERC order. This Letter Agreement does not purport to assign responsibility for the Underscheduling Penalty to either Party hereunder</i>
7. Interest: Interest associated with all principal amounts which were past due prior to January 17, 2001 (including those items described in Exhibit A-1) or interest associated with principal amounts for which SCE is the responsible party as set forth in this Exhibit A-2, including interest assessed to SCE by the ISO as part of Neutrality Charge Type 1010.	SCE
8. Charges for Non-Retail Load: This includes all charges assessed by the ISO to SCE for SCE's existing transmission contracts and all charges except 407-Uninstructed Energy and 487-Allocation of Excess Cost for Uninstructed Energy for SCE's Power Contracts' load which is served by SCE's generation and contracts. Charges for 407-Uninstructed Energy and 487-Allocation of Excess Cost for Uninstructed Energy for such Power Contracts' load shall be paid by CDWR.	SCE
9. Reliability Must Run related payments or charges: This includes charges associated with RMR unit operations. To the extent SCE's RMR generation is not operated according to contract, SCE will be financially responsible for charges assessed by the ISO for SCE's failure to perform contractual obligations. (For example, CT 410, RMR Imbalance Energy Payment Withheld for Unscheduled RMR energy.)	SCE
10. Transmission Owner Related Payments or Charges: SCE is entitled to payments or billing adjustments related to congestion refunds due TO. (CT 204	SCE

Charge	Responsible Party
and 254). SCE has separate SC agreements to account for TO payments and charges. To the extent the ISO has credited or debited TO related charges to CERS, these payments and charges rightfully belong to the TO function of SCE.	
11. Voltage Support: Costs associated with Voltage Support, CT 1302 Long Term Voltage Support, less any payments received by SCE for providing Voltage Support, including but not limited to CT 3303-Long Term Voltage Support Due SC. This category shall also include costs associated with Supplemental Reactive Energy, CT 1303-Supplemental Reactive Energy due ISO, less any payments received by SCE for providing supplemental reactive energy, including by not limited to CT 302-Supplemental Reactive Power due SC and CT 3302-Supplemental Reactive Energy Due SC.	SCE
12. Any other charges: To the extent additional charges are billed to SCE or developed by ISO, CERS and SCE will analyze these charges to determine if they are third-party transactions to be credit-backed by CERS.	<i>The responsible party for these charges shall be determined pursuant to Section 2 of the Letter Agreement</i>

EXHIBIT B

Imbalance Energy Catch-Up Payable

Payments for the Imbalance Energy for the Catch-Up Period shall be remitted as described in this Exhibit B.

DWR and SCE shall agree on the kilowatt-hours of Imbalance Energy bought or sold for SCE's retail customers by the ISO for each hour of the Catch-Up Period. With respect to such quantification of Imbalance Energy, Section 3 of this Letter Agreement regarding the treatment of Instructed Imbalance Energy shall apply.

For the purposes of this Letter Agreement, Imbalance Energy shall include Uninstructed Energy quantities reflected in ISO's Charge Type 407. Instructed Energy (also referred to herein as Instructed Imbalance Energy) quantities reflected in ISO's Charge Type 401 shall be included or excluded from Imbalance Energy as provided in Section 3 of this Letter Agreement. Notwithstanding the foregoing, Uninstructed Energy (Charge Type 407) and Instructed Energy (Charge Type 401) bought or sold by SCE in connection with its Existing Transmission Contracts shall not be considered Imbalance Energy hereunder.

SCE shall determine the weighted-average Distribution Loss Factor for each hour of the Catch-Up Period ("Hourly DLF") as follows: subtract (a) SCE's aggregated retail usage from (b) SCE's retail usage reported to the ISO, which is aggregated retail usage grossed retail usage reported to the ISO.

SCE shall multiply the kilowatt-hours of Imbalance Energy bought or sold for SCE's retail customers by the ISO by the factor of one minus the Hourly DLF to determine the "Hourly Imbalance Energy Purchases/Sales At Retail." For each day of the Catch-Up Period, SCE shall net the Hourly Imbalance Energy Purchases/Sales At Retail to determine the "Daily Imbalance Energy Purchases/Sales At Retail."

SCE shall multiply the Daily Imbalance Energy Purchases/Sales At Retail by the rate that SCE paid DWR for Scheduled Energy delivered that day and by a factor of one minus of the applicable CPUC authorized uncollectibles factor, which represents the fraction of SCE bills which is not collectable from retail customers, to determine the "Daily Imbalance Energy Payable/Receivable." SCE shall net the Daily Imbalance Energy Payable/Receivable for each day of the Catch-Up Period to determine the "Imbalance Energy Catch-Up Payable Before Interest" due to DWR.

SCE shall provide DWR with work papers to validate SCE calculations of DLFs and uncollectibles.

The Parties acknowledge that as of the date of the execution of this Letter Agreement, ISO settlement statements will not be available for all days of the Catch-up Period. The Parties agree, therefore, that the above calculations will be trued-up and revised as necessary as ISO settlement statements become available for the entire Catch-up Period. Such true-up payments described in this provision shall be made on July 1, 2002.

EXHIBIT C

Total Offsets

Offsets for the period January 17, 2001 through June 2, 2001 (“Adjustment Period”).

SCE shall calculate the following offsets and provide DWR with appropriate work papers to validate SCE’s calculations:

C.1 Loss Adjustment For Scheduled Energy for the Adjustment Period.

Prior to June 3, 2001, SCE’s retail customers paid CDWR for Scheduled Energy that was not adjusted for distribution losses. The Loss Adjustment For Scheduled Energy is intended to compensate SCE for payments that SCE previously made to CDWR for Scheduled Energy that was not delivered to SCE’s retail customers as a result of distribution losses.

The “Hourly Loss Adjustment For Scheduled Energy” shall be determined by multiplying the Scheduled Energy for which CDWR was paid by SCE for each hour of the Adjustment Period by the Hourly DLF and by the rate (in dollars per megawatt-hours) CDWR was paid for such Scheduled Energy.

The “Loss Adjustment For Scheduled Energy” shall be determined by summing the Hourly Loss Adjustment For Scheduled Energy over all hours of the Adjustment Period.

C.2 Uncollectibles Adjustment For Scheduled Energy for the Adjustment Period.

Prior to June 3, 2001, SCE paid CDWR for Scheduled Energy deliveries to retail customers, for which SCE may not have been paid by retail customers. The Uncollectibles Adjustment For Scheduled Energy is intended to compensate SCE for payments that SCE previously made to CDWR for Scheduled Energy, but did not receive from its retail customers.

The “Hourly Adjusted Scheduled Energy Payable” shall be determined by multiplying the Scheduled Energy for which CDWR was paid by SCE for each hour of the Adjustment Period by a factor of one minus the Hourly DLF and by the rate (in dollars per megawatt-hours) that CDWR was paid for such Scheduled Energy.

The “Hourly Uncollectibles Adjustment For Scheduled Energy” shall be determined by multiplying the Hourly Adjusted Scheduled Energy Payable by a factor of one minus the applicable CPUC authorized uncollectibles factor.

The “Uncollectibles Adjustment For Scheduled Energy” shall be determined by summing the Hourly Uncollectibles Adjustment For Scheduled Energy over all hours of the Adjustment Period.

C.3 Total Offsets.

The sum of the Loss Adjustment For Scheduled Energy and the Uncollectibles Adjustment For Scheduled Energy shall be defined as the “Total Offsets.”

EXHIBIT D

SCE'S EXISTING TRANSMISSION CONTRACTS AND POWER CONTRACTS

Transmission Contracts
AEPCo Firm Transmission Service Agreement
APS Firm Transmission Service Agreement (Blythe)
Firm Transmission Service Agreement (Eldorado-Vincent)
IID Firm Transmission Service Agreement
Eldorado System Transmission Rights And Curtailments
LADWP Exchange Agreement
US Bureau Of Reclamation Navajo Transmission Agreement
MATA Agreement (MKP-MCC WHEEL)
MSR Firm Transmission Service Agreement
PacificCorp Transmission Service Agreement
Mohave Project Co-Tenancy Agreement
Power Contracts
AEPCo Load Control Agreement
BPA Sale AND Exchange Agreement
BPA Environmental Energy Storage Agreement
CDWR Power Contract
CDWR Capacity Exchange Agreement
Edwards AFB Revised Power Displacement Agreement
March AFB Power Allocations FROM Agreement
Metropolitan Water District Service AND Interchange Agreement
Metropolitan Water District Etiwanda Transmission Service Agreement
NEVP Power Purchase Agreement
PacificCorp Long Term Power Sales Agreement
PacificCorp Winter Power Sale Agreement
TEP Power Exchange Agreement
Valley Electric Exchange Agreement
Boulder Canyon Project